

BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF HAWAII

-----In the Matter of----- ) DOCKET NO. 2008-0274  
 )  
PUBLIC UTILITIES COMMISSION )  
 )  
Instituting a Proceeding to )  
Investigate Implementing a )  
Decoupling Mechanism for Hawaiian )  
Electric Company, Inc., Hawaii )  
Electric Light Company, Inc., and )  
Maui Electric Company, Limited. )  
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THE DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT, AND TOURISM'S  
RESPONSES TO THE PUBLIC UTILITY COMMISSION'S INFORMATION  
REQUESTS

AND

CERTIFICATE OF SERVICE

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**THE DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT, AND TOURISM'S  
RESPONSES TO THE PUBLIC UTILITY COMMISSION'S INFORMATION  
REQUESTS**

The Department of Business, Economic Development, and Tourism  
("Department" or "DBEDT"), by and through its Director  
("Director") in his capacity as the Energy Resources  
Coordinator, through the undersigned Deputy Attorney General,  
hereby submits to the Hawaii Public Utilities Commission  
("Commission" or "PUC") its responses to the Commission's  
information requests issued on March 5, 2009.

**PUC IRs for other Parties:**

24. At the technical workshop, the participants discussed that the proposed decoupling adjustment would create a bias for the utility to overstate test-year sales and for rate increase opponents to understate test year sales. Please discuss.

**DBEDT Resposne:**

24. During the technical workshop, the HECO Companies, the Consumer Advocate ("CA"), and Haiku Design and Analysis ("HDA") presented their respective decoupling mechanism proposals. The HECO Companies' and the CA's decoupling proposals are based on a method that determines the utilities' target revenue requirements for post test-year periods (i.e., in between rate cases), by simply escalating the utilities' operation and maintenance costs (O&M costs) and rate base. This method of determining target revenue requirements, independent of the utilities' kilowatt-hour sales, effectively decouples the utilities' revenues (and therefore profits) from its kilowatt-hour sales. The method of determining the target revenue requirements for the post test-year periods (i.e., in between rate cases) is referred to by the parties as the Revenue Adjustment Mechanism ("RAM").

During the technical workshop, there was limited discussion on some perceived biased effect on decoupling of test-year sales that, to DBEDT's recollection, was brought

about by some questions on "marginal" fuel costs and the ECAC by HDA. DBEDT's observation is that questions were raised because the ECAC calculation and its relationship to the fuel costs embedded in the utilities' base rates are not clear to some parties, such as HDA. However, in both the CA's and the HECO Companies' proposals, the fuel costs and purchased power expense recovered through the ECAC are excluded from the O&M costs that the parties proposed to escalate, and are instead maintained at the allowed level in the baseline test-year (i.e., 2009) that will be used for the decoupling.

Under traditional ratemaking, the forecast of a utility's sales is the major basis for determining the utility's required revenue requirements and the amount of proposed rate increase. It is the basis for the utility's estimates of some of test-year O&M costs as well, such as fuel costs. It is also the basis for the utility's determination of its test-year revenues at present rates, which is critical in determining the amount of the required or proposed total revenue requirements and therefore the amount of requested rate increase.

Under the decoupling mechanism proposed by both the CA and the HECO Companies, the utility's sales are not a consideration in determining the target revenue

requirements for the post test-year periods (i.e., in between rate cases). Thus, based on the initial decoupling method being proposed by HECO and the CA, DBEDT does not believe that decoupling would create a bias for the utility to overstate test-year sales and for rate increase opponents to understate test-year sales. However, DBEDT's position on this matter may change based on more detailed information that may be provided by the parties during the proceeding.

25. Sales decoupling, the RAM and REIS as proposed, each either reduce total risk or shift the risk of a utility not achieving the authorized rate of return to customers. Given the changes in risk associated with these revenue adjustment mechanisms please explain:

- a. Why should the utility be allowed to retain any earnings in excess of the authorized rate of return rather than these earnings in excess of the authorized level being allocated to the benefit of customers? Please suggest a mechanism that could allocate these earnings to customers?
- b. Please discuss the effect the reduction and shift in risk should have on the utilities' authorized rate of return.

**DBEDT Response:**

25.a. DBEDT agrees with the Commission that decoupling and the REIS both reduce the total risk of a utility not achieving the authorized rate of return or shift that risk to the ratepayers. DBEDT also believes that to the maximum extent

possible, any earnings achieved by the utility in excess of the authorized rate of return should be allocated to the benefit of the customers. However, DBEDT also believes that allowing the utility to retain a small portion of the achieved earnings in excess of the authorized return may provide the utility an incentive to manage costs. One major concern relating to the HECO Companies' proposed decoupling mechanism is that the utilities do not have any incentive to manage their costs since their proposal allows them automatic unlimited annual rate increases that pass their forecasted costs increases to the ratepayers whatever they may be. By allowing them to retain a small portion of any excess earnings they achieve, it may incentivize them to manage their costs to maximize those excess earnings in which they could partake.

The CA's proposed decoupling mechanism includes an earnings sharing mechanism similar to the HECO proposal in Docket No. 99-0396, which merits the PUC's consideration. The percentage shares may be adjusted by the PUC in consideration of the impact on the utility's earnings of REIS, and the other incentives supported by the Parties in the Energy Agreement that are subject to PUC approval. DBEDT recognizes that even with such an earnings sharing mechanism, it is uncertain that the utility will manage its

costs under the proposed RAM. In DBEDT's statement of position, DBEDT recommended several consumer protection measures to incorporate in the decoupling design, including imposing caps on the amount of annual rate increase and most importantly, relating the allowed amount of rate increase to the performance metrics suggested by DBEDT.

25.b. The reduction in the utility's risk resulting from decoupling would decrease the utility's financing costs which should then lower its required rate of return. The lower required rate of return will result in lower revenue requirements and hence, a lower rate increase. DBEDT does not have an estimate of the impact of decoupling on the utility's required rate of return.

26. Please compare the regulatory costs associated with the proposed RAM and the rate cases every two years.

**DBEDT Response:**

26. DBEDT does not have an estimate of the regulatory costs associated with the proposed RAM. However, DBEDT believes that in comparison with holding rate cases every two years, the regulatory costs of the proposed RAM could be lower, based on the volume of material that is normally required and filed by the utilities in rate cases as compared to

what may be required under the proposed RAM. It should be noted however that the RAM procedure proposed by both the CA and the HECO Companies requires that the utilities file rate cases every two years.

DATED: Honolulu, Hawaii, March 30, 2009.

  
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Certificate of Service

I hereby certify that I have served a copy of the Department of Business, Economic Development, and Tourism's Responses to the PUC's Information Requests Issued on March 5, 2009, in Commission Docket Number 2008-0274, by electronic transmission on the date of signature to each of the parties listed below.

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